INTERCO
1989 ANNUAL REPORT

INTERCO Today is a broadly based major manufacturer and retailer of footwear and furniture products and services represented by two operating groups.

Footwear Manufacturing and Retailing Group styles, manufactures and distributes primarily men's footwear, and a broad range of athletic footwear, principally in the United States, Australia, Canada and Mexico. There are nine manufacturing plants and five major distribution centers in operation. The group operates 743 retail shoe stores and leased shoe departments in 40 states in this country, as well as in Australia, Canada and Mexico. Footwear products are also distributed in more than 85 foreign countries.

Furniture and Home Furnishings Group manufactures and distributes quality furniture and home furnishings. There are 64 factories and 17 major distribution centers and consolidation warehouses located throughout the United States. The company also owns and operates 34 galleries.

Contents

Overview

(Dollars in thousands except per share data)

Years Ended	**February 25, 1989**	February 29, 1988
From operations:		
Net sales	**$ 2,011,962**	$ 1,995,974
Net earnings (loss):		
Continuing operations	**(4,282)**	113,434
Discontinued operations	**74,432**	31,569
Total	**$ 70,150**	$ 145,003
Earnings (loss) per share:		
Continuing operations	**$ (0.42)**	$ 2.74
Discontinued operations	**1.95**	0.76
Total	**$ 1.53**	$ 3.50
Financial Condition:		
Working capital	**$ 451,609**	$ 985,956
Current ratio	**1.6 to 1**	4.7 to 1
Total assets	**1,775,302**	1,830,400
Shareholders' equity (deficit)	**(1,005,750)**	1,251,337
Shares outstanding at year end:		
Common	**37,863,035**	36,183,036
Preferred:		
Series D	**19,103**	571,133
Series E	**3,320,702**	—
Number of shareholders	**8,000**	12,500

To Our Shareholders:

During fiscal year 1989 major changes were forced upon INTERCO INCORPORATED. In the first half of the year we continued to make steady progress on the company's strategic repositioning program that was initiated several years earlier. However, in July INTERCO received an unsolicited, hostile takeover bid which the board of directors, on the advice of its financial and legal advisors, concluded was inadequate and not in the best interests of the shareholders. Subsequently, the company implemented a major recapitalization and restructuring program under which the following special dividends were declared, thereby dramatically changing the financial structure of the company:

- Cash dividends of $1.42 billion;
- $404 million of 13¾ percent senior subordinated debentures, maturing December 15, 2000;
- $386 million face amount of 14 percent subordinated discount debentures, maturing December 15, 2003;
- $213 million face value of 14½ percent junior pay-in-kind debentures, maturing December 15, 2003;
- $342 million of 17½ percent Series E preferred stock, with each share including 3.5 warrants to purchase INTERCO common stock.

To help fund these special dividends, as well as other costs associated with the restructuring, INTERCO entered into a $1.915 billion Secured Credit Agreement with a bank syndicate which included a $1.15 billion asset sale bridge loan facility to be repaid over 18 months.

Asset Sales

To repay the bridge loan portion of the Secured Credit Agreement, INTERCO has embarked on an asset sale program calling for the divestiture of the Apparel Manufacturing and General Retail Merchandising Groups, as well as Ethan Allen Inc. and Senack Shoes, Inc. To date, we have completed the sale of Londontown, The Biltwell Company, International Hat Company, and have reached agreement to sell Big Yank Corporation and Cowden Manufacturing Company. Total net proceeds from these sales will approximate $250 million. Following completion of the asset sale program, INTERCO will be comprised of four core companies: Broyhill Furniture Industries, Inc. and The Lane Company, Incorporated in the furniture segment, and Converse Inc. and The Florsheim Shoe Company in the footwear sector. They are four of INTERCO's strongest and best managed operating companies.

Core Company Profiles

Broyhill, founded in 1926, produces popular priced bedroom, dining room, living room and occasional products in a wide range of styles. A leader in manufacturing automation, Broyhill is an extremely efficient producer in its market segment. In the past few years, the company has made significant strides with innovative marketing strategies. Its leading Showcase Gallery program, for example, has expanded to approximately 280 retail locations, and an aggressive growth program is planned for this year.

For the smaller retailer, the independent dealer program was launched, which provides professionally coordinated, year-round advertising and promotional planning. This pioneering effort currently has more than 500 retail locations enrolled in 44 states, Canada and Bermuda, and the number of participating dealers is expected to double over the next few years. The company is also increasing market penetration with its Contract Division, supplying furnishings for hotels, motels and health care facilities. Additional programs, targeting department stores, national and regional furniture chains, have also met with positive response.

Lane is a highly respected name in the furniture industry. Founded in 1912 as a cedar chest maker, it broadened its product mix dramatically through both internal growth and acquisitions. Today, the company is still renowned for its cedar chests, and also for occasional and living room furniture, bedroom and dining room furniture, entertainment cabinets, and other fine, crafted products which are marketed under the Lane trademark. Lane is the nation's second largest manufacturer of recliners through its Action Industries subsidiary. Hickory Chair is well known

for its *James River* collection of dining room, bedroom and occasional furniture and the recently introduced *Mark Hampton* collection. Other divisions include Venture with outstanding rattan offerings; Pearson's quality upholstered furniture, and HBF, with fine quality office furniture. Lane has initiated its own focused gallery program, which currently totals some 35 locations and represents an additional avenue of growth.

■ Converse is the largest manufacturer and the third largest supplier of athletic footwear in the United States. Best known for its basketball shoes, Converse also markets a broad range of footwear designed for running, racquet and field sports. Its products are endorsed by such well known athletes as Larry Bird, Magic Johnson, Jimmy Connors, Chris Evert, Bernie Kosar and Don Mattingly. The *Converse Chuck Taylor All Star* canvas shoe has produced sales of over 500 million pairs, by far the largest selling athletic shoe, and still going strong. Children's shoes and international sales are also showing good growth potential. Converse's research and development efforts produced the *Energy Wave*, and since its introduction in the summer of 1988, is generating substantial interest in the industry. This innovation, which has applications in a wide range of athletic footwear, incorporates a proprietary chemical polymer that will return up to 70 percent more energy to the wearer than the performance shoes of leading competitors.

■ Florsheim, a leading manufacturer and retailer of men's dress and dress/casual footwear for 97 years, currently has better than a 20 percent market share, the largest of any competitor. The company recently broadened its product line with the introduction of *ComforTech*, representing a strong thrust into casual footwear. It markets women's shoes through the Florsheim Thayer-McNeil company-operated stores, as well as through independent retailers. During the year the International Shoe Company, best known for its *Hy-Test* safety shoe, was consolidated into Florsheim.

Florsheim's wholesale distribution, currently serving over 5,000 independent dealers, is undergoing a change as the company expands its focus on retailers in smaller markets, notably strip centers and malls in mid-sized cities. The *Express Shop* program with its in-store computer console offering every style and color in Florsheim's product line is growing. The company will soon have installations in 500 locations. Benefits include positive consumer reaction, increased sales potential, and minimal inventory requirements.

Cost Savings Program

INTERCO has initiated a cost savings and operating efficiencies program with an annual target of $75 million. Cost reductions are being implemented on a broad scale throughout the four core companies and corporate headquarters and we believe excellent progress has been made toward this initial goal. We are mindful of the effect of the cost-reduction program on all of our corporate constituencies, and have acted to minimize the impact of these actions to the extent possible.

Fiscal 1989 Results

Numerous costs related to the restructuring significantly impacted operating results for the year ended February 25, 1989. Net sales from continuing operations rose slightly to $2.01 billion from $2.00 billion one year ago. Net earnings, including discontinued operations, were $70.2 million, compared with $145.0 million in the prior year. Fiscal 1989 net profits were affected by $104.1 million of interest expense ($69.1 million, net of income tax) related to the restructuring, as well as by $14.0 million of nondeductible restructuring costs and expense. A net after tax gain of $34.3 million was recorded from the sale of assets. Earnings per share, including discontinued operations, were $1.53, after preferred dividend requirements of $11.8 million, or $0.30 per share, compared with $3.50 last year.

Sales of the Furniture and Home Furnishings Group were about even—$1.10 billion, compared with $1.11 billion one year ago. Operating earnings declined 11.6 percent to $131.7 million from $149.1 million the prior year, which was a record for the Furniture Group.

Recent order patterns have been strong at Broyhill and Lane and both companies had excellent reception to their products at the April 1989 Furniture Market. Backlogs are running ahead of last year.

Sales of the Footwear Manufacturing and Retailing Group rose 2.8 percent to $915.5 million from $890.4 million in the prior year. Operating earnings declined to $45.6 million from a record $92.2 million the year before. Contributing to the decrease were soft sales and increased promotional costs in the fashion segment of Converse's canvas footwear; manufacturing start-up expenses within the performance athletic footwear segment and one-time costs approximating $10.4 million for plant closings and realignments within the men's traditional footwear operations. Incoming order trends are also strengthening in the Footwear Manufacturing and Retailing Group, notably demand for Converse's performance basketball shoes. Domestic orders for canvas footwear have stabilized, although the international canvas business remains soft. Both Converse and Florsheim should benefit from refocusing their merchandising efforts to take advantage of the many strengths of their product lines. In addition, Florsheim will begin to realize the benefits of last year's consolidation of the International Shoe Company.

Management, Board Changes

In March 1989, Richard B. Loynd, formerly chairman of Converse, was elected president and chief operating officer of INTERCO, succeeding Harry M. Krogh, who retired as an officer and Director of the company. Mr. Loynd brings strong management expertise and experience in operating in a highly leveraged environment. Eugene F. Smith, formerly senior vice president, finance at INTERCO, was promoted to executive vice president and continues as chief financial officer. Mark H. Lieberman, president of Londontown, resigned as a Director and vice president of INTERCO upon the sale of Londontown.

Outlook

While this past year has been extraordinarily difficult and challenging, INTERCO will emerge from this basic restructuring as a more focused company, with operations that are industry leaders having strong consumer brands. In addition, each of the core companies has an experienced management team, working in partnership with thousands of dedicated, skilled employees who have significant stakes in the ongoing success of their respective businesses. They have played a major role in positioning their companies as market leaders and will continue to do so; their efforts are greatly appreciated. Throughout the corporation there is a commitment to growing these core businesses. Within the framework of our existing financial structure, each company is continually evolving strategies for further growth, including innovative products, essential for the long-term viability of INTERCO. Our aggressive cost-reduction program will help enhance profit margins. Progress has been encouraging and we may be able to surpass the initial $75 million cost savings goal.

On behalf of INTERCO's Board of Directors and management, we would like to express our appreciation to our shareholders for your support and understanding, as well as our appreciation to our customers and suppliers.

Harvey Saligman
Chairman of the Board and Chief Executive Officer
April 28, 1989

Management's Discussion and Analysis of Results of Operations and Financial Condition

RESULTS OF OPERATIONS

This discussion supplements the detailed information presented in the consolidated financial statements and footnotes which begin on page 8.

Results for fiscal 1989, 1988 and 1987 are restated to account for the Apparel Manufacturing and General Retail Merchandising Groups as discontinued operations.

Net Sales

Net sales for fiscal 1989 were $2.01 billion, an increase of 0.8% from the $2.00 billion last year. Net sales for fiscal 1988 increased 22.4% from the $1.63 billion in fiscal 1987. For fiscal 1989, sales for the Footwear Manufacturing and Retailing Group recorded a modest increase from the prior year, despite a decline in the fashion segment of canvas footwear at Converse, as well as the impact of the realignment of the International Shoe Company into Florsheim. The Furniture and Home Furnishings Group's sales decreased slightly from the strong results in the prior year. For fiscal 1988, sales of the Footwear and Furniture Groups increased by 34.2% and 14.3%, respectively. The Footwear Group results benefited from a significant increase at Converse, together with smaller gains at the other footwear companies. Within the Furniture Group, each company experienced solid gains over the prior year.

Other Income, Net

Other income for fiscal 1989 was $18.9 million, an increase of $5.2 million from the prior year, which was down slightly from the fiscal 1987 level. The increase in fiscal 1989 was due mainly to the sale of marketable investment securities.

Gross Margins

Gross margins for fiscal 1989 were $676.3 million, or 33.6% of net sales, as compared to $707.2 million, or 35.4% and $579.8 million, or 35.6% for fiscal 1988 and 1987, respectively. Margins in fiscal 1989 were adversely impacted by the results of the Footwear Manufacturing and Retailing Group due to promotional costs and unfavorable manufacturing variances resulting from the sales decline in canvas footwear, manufacturing start-up costs within the athletic footwear segment, and costs associated with plant closings and realignments within the men's traditional footwear segment. The Furniture Group's gross margins were about even with the prior year. For fiscal 1988, the Footwear Manufacturing and Retailing Group showed improved gross margins while the Furniture and Home Furnishings Group's margins were level as a percent of sales, but up substantially in absolute amount. The improvement in fiscal 1987 consolidated gross margins was principally attributable to higher gross margins in the Furniture Group.

Selling, General and Administrative Expenses

Selling, general and administrative expenses were $523.8 million, $493.0 million and $415.9 million for fiscal 1989, 1988 and 1987, respectively. As a percent of sales, selling, general and administrative expenses were 26.0% for fiscal 1989, as compared to 24.7% for fiscal 1988 and 25.5% for fiscal 1987.

The increase in fiscal 1989 was primarily attributed to promotional, marketing and realignment costs within the Footwear Group.

Interest Expense
Interest expense in fiscal 1989 totaled $141.7 million, compared to $29.2 million in fiscal 1988 and $23.1 million in fiscal 1987. The increase in fiscal 1989 was attributable to the $104.1 million in interest cost related to the restructuring program and interest on the $200.0 million of long-term debt issued in the fourth quarter of the prior year. The increase in fiscal 1988 was due mainly to higher levels of short-term borrowings associated with the company's share repurchase programs, and also as a result of the debt initially incurred for the acquisition of Converse.

Restructuring Expenses
In the third quarter, a one-time charge of $14.0 million for restructuring expenses, which are nondeductible for income tax purposes, was incurred.

Earnings From Continuing Operations Before Income Taxes
Earnings from continuing operations were $15.7 million, as compared to $198.7 million and $154.8 million in fiscal 1988 and 1987, respectively. Earnings were adversely impacted by interest expense and other costs incurred in the company's restructuring program, in addition to the operating and realignment costs and expenses noted above. The increase in fiscal 1988 over fiscal 1987 was attributable to the strong earnings improvement for both the Footwear and Furniture Groups.

Income Taxes
Income taxes in fiscal 1989 were $20.0 million and exceeded the pretax earnings from continuing operations due to the nondeductible expenses incurred, including the restructuring expenses. For fiscal 1988 and 1987 the effective tax rate was 42.9% and 46.1%, respectively. The decrease in the effective tax rate in fiscal 1988 was due to the reduction in the corporate income tax rate in the 1986 Tax Reform Act.

Adoption of Financial Accounting Standards Board Statement No. 96, Accounting for Income Taxes, will result in a cumulative tax adjustment that may be reported in income in the year of implementation. The company is currently studying the provisions of FAS 96 and has not yet decided when it will be adopted, or the method of adoption.

Discontinued Operations
Net earnings from discontinued operations were $74.4 million, $31.6 million and $42.3 million in fiscal 1989, 1988 and 1987, respectively. Included in discontinued operations are the results of operations of the Apparel Manufacturing and General Retail Merchandising Groups. In addition, fiscal 1989 included goodwill charges related to the two groups, and the gain recognized on the sale of Londontown and other assets. These operations are discussed in more detail in Note 3 to the Consolidated Financial Statements.

Earnings Per Share
The loss per share from continuing operations was $0.42, as compared to earnings of $2.74 in fiscal 1988 and $1.93 in fiscal 1987.

Earnings per share, including discontinued operations were $1.53, $3.50 and $2.91 in fiscal 1989, 1988 and 1987, respectively.

Earnings per share in fiscal 1989 were reduced by the preferred stock dividend requirements of $11.8 million, or $0.30 per share, on the Series E stock issued as a dividend in the restructuring.

Average shares utilized in the calculation of earnings per share were 38,262,000 in fiscal 1989, 41,456,000 in fiscal 1988 and 43,312,000 in fiscal 1987.

FINANCIAL CONDITION

Working Capital

Working capital, the excess of current assets over current liabilities, was $451.6 million at the end of fiscal 1989, as compared to $986.0 million in fiscal 1988 and $928.4 million in fiscal 1987. The current ratio was 1.6 to 1, 4.7 to 1 and 5.0 to 1 in fiscal 1989, 1988 and 1987, respectively.

The decrease in working capital was due to the inclusion of $499.8 million of current maturities of debt generated in the restructuring. The company plans to repay this debt from proceeds of asset sales as part of the restructuring.

Financing Arrangements

The company replaced the revolving credit agreements which existed in fiscal 1988 with a new Secured Credit Agreement. The new agreement, more fully described in Note 6 to the Consolidated Financial Statements, provided the financing for the cash portions of the dividends. The agreement provides for the seasonal working capital and letters of credit needs of the company, and contains certain covenants, including capital expenditures, rental obligations and interest coverage. At February 25, 1989, the company was not in compliance with the coverage ratio and the interest coverage ratio covenants. The bank syndicate has granted temporary waivers in this regard.

The company expects to meet its debt service, principal repayment and operating cash needs through cash generated by the company's operations, from proceeds of asset sales and from available credit obtained to support the restructuring.

Capital Expenditures

Capital expenditures in fiscal 1989 were $53.8 million, as compared to $45.9 million in the prior year. Depreciation expense was $40.0 million, as compared to $40.6 million in fiscal 1988. For fiscal 1990, capital expenditures are projected to be $35.0 million.

Dividends

Cash dividends of $1,453.3 million, including $1.9 million on the Series D preferred stock and $0.9 million on the common stock rights redemption were paid during fiscal 1989. In addition, non-cash dividends of $1,003.1 million, representing Series E preferred stock and debt securities were distributed.

No dividends will be paid on the company's common shares for the foreseeable future.

Shares Repurchased

During the first half of fiscal 1989, the company purchased 2.2 million shares of its outstanding common stock for $102.3 million in conjunction with its Share Repurchase Program.

Consolidated Balance Sheet

(Dollars in thousands except per share data)

Assets	February 25, 1989	February 29, 1988	February 28, 1987
Current assets:			
Cash	**$ 16,308**	$ 12,476	$ 8,837
Marketable securities	**61,317**	10,823	63,747
Receivables, less allowances of $10,599 ($10,606 in 1988 and $11,516 in 1987)	**329,299**	310,053	264,458
Inventories	**490,967**	514,193	432,794
Prepaid expenses and other current assets	**41,625**	24,984	16,304
Net current assets of discontinued operations held for sale	**248,361**	382,742	374,392
Total current assets	**1,187,877**	1,255,271	1,160,532
Net noncurrent assets of discontinued operations held for sale	**98,011**	138,902	143,858
Property, plant and equipment:			
Land	**19,105**	18,454	17,836
Buildings and improvements	**321,591**	297,876	284,571
Machinery and equipment	**257,043**	252,281	234,388
	597,739	568,611	536,795
Less accumulated depreciation	**270,669**	251,373	224,013
Net property, plant and equipment	**327,070**	317,238	312,782
Other assets	**162,344**	118,989	124,637
	$1,775,302	$1,830,400	$1,741,809

See accompanying notes to consolidated financial statements.

Liabilities and Shareholders' Equity	**February 25, 1989**	February 29, 1988	February 28, 1987
Current liabilities:			
Notes payable	**$ 6,017**	$ 70,517	$ 68,840
Current maturities of long-term debt and capital lease obligations	**509,961**	4,816	7,686
Accounts payable	**99,231**	105,165	78,084
Accrued employee compensation	**27,317**	33,021	28,101
Accrued interest	**35,339**	3,568	3,019
Other accrued expenses	**53,618**	35,622	29,612
Income taxes	**4,785**	16,606	16,763
Total current liabilities	**736,268**	269,315	232,105
Long-term debt, less current maturities	**1,169,929**	257,327	134,642
Debentures	**808,657**	—	—
Obligations under capital leases, less current maturities	**8,251**	8,864	8,716
Other long-term liabilities	**57,947**	43,557	40,131
Shareholders' equity:			
Preferred stock, authorized 10,000,000 shares:			
Series D, no par value,—issued 19,103 shares in 1989, 571,133 shares in 1988 and 617,946 shares in 1987	**1,910**	57,113	61,795
Series E, $1.00 stated value, issued 3,320,702 shares in 1989	**3,321**	—	—
Common stock, $3.75 stated value, authorized 125,000,000 shares—issued 41,356,847 shares in 1989 and 1988, and 43,638,211 shares in 1987	**155,088**	155,088	163,643
Capital surplus	**179,337**	44,539	98,246
Retained earnings (deficit)	**(1,208,250)**	1,179,964	1,099,006
	(868,594)	1,436,704	1,422,690
Less 3,493,812 (5,173,811 and 3,464,957 in 1988 and 1987, respectively) shares of common stock in treasury, at cost	**137,156**	185,367	96,475
Total shareholders' equity (deficit)	**(1,005,750)**	1,251,337	1,326,215
	$ 1,775,302	$1,830,400	$1,741,809

Consolidated Statement of Earnings

(Dollars in thousands except per share data)

Years Ended	February 25, 1989	February 29, 1988	February 28, 1987
Income:			
Net sales	**$2,011,962**	$1,995,974	$1,630,918
Other income, net	**18,943**	13,714	13,981
	2,030,905	2,009,688	1,644,899
Costs and expenses:			
Cost of sales	**1,335,678**	1,288,748	1,051,110
Selling, general and administrative expenses	**523,797**	493,015	415,923
Interest expense	**141,735**	29,188	23,061
Nondeductible restructuring expenses	**14,000**	—	—
	2,015,210	1,810,951	1,490,094
Earnings from continuing operations before income taxes	**15,695**	198,737	154,805
Income taxes	**19,977**	85,303	71,321
Net earnings (loss) from continuing operations	**(4,282)**	113,434	83,484
Discontinued operations (net of taxes of $55,047 in 1989, $23,154 in 1988 and $40,616 in 1987, respectively)	**74,432**	31,569	42,290
Net earnings	**$ 70,150**	$ 145,003	$ 125,774
Earnings per share:			
Continuing operations	**$(0.42)**	$2.74	$1.93
Total earnings	**$ 1.53**	$3.50	$2.91

See accompanying notes to consolidated financial statements.

Consolidated Statement of Cash Flows

(Dollars in thousands)

Year Ended	February 25, 1989
Cash Flows from Operating Activities:	
Net loss from continuing operations	$ (4,282)
Adjustments to reconcile net income to net cash provided by operating activities:	
Depreciation and amortization	74,201
Decrease in deferred income taxes	(12,955)
Net increase in deferred items	(45,439)
Minority interest in net income	605
Increase in accounts payable and accrued expenses	37,479
Increase in accounts receivable	(19,246)
Decrease in inventory	23,226
Increase in prepaid expenses	(76)
Decrease in Federal income taxes payable	(11,821)
Increase in other assets	(1,152)
Net cash provided by operating activities of continuing operations	40,540
Net cash provided by discontinued operations	249,704
Net cash provided by operating activities	290,244
Cash Flows from Investing Activities:	
Proceeds from the sale or disposal of property, plant, equipment and leasehold interests	4,134
Additions to property, plant, equipment and leasehold interests	(50,966)
Net cash used by investing activities	(46,832)
Cash Flows from Financing Activities:	
Proceeds from the sale or issuance of common stock	19,994
Payments to acquire treasury stock	(102,341)
Dividends paid	(1,456,162)
Proceeds from issuance of long-term debt	1,967,500
Reduction of long-term debt	(614,071)
Decrease in obligations under capital lease	(3,330)
Other	(676)
Net cash used in financing activities	(189,086)
Net increase in cash and cash equivalents	54,326
Cash and cash equivalents at beginning of year	23,299
Cash and cash equivalents at end of year	$ 77,625
Supplemental disclosure:	
Cash payments for income taxes	$ 52,067
Cash payments for interest, net of amounts capitalized	$ 73,926

See accompanying notes to consolidated financial statements.

Consolidated Statement of Changes in Financial Position

(Dollars in thousands)

Years Ended	February 29, 1988	February 28, 1987
Working capital provided by:		
Net earnings	$145,003	$125,774
Items not affecting working capital:		
Depreciation	40,570	35,032
Other, net	8,750	16,297
Operations	194,323	177,103
Disposal of property, plant and equipment	1,145	4,129
Issuance of common stock	4,606	11,540
Additions to long-term debt	200,000	253
Additions to capital lease obligations	5,533	196
To conform pooled companies fiscal year	—	2,363
Other, net	252	—
	405,859	195,584
Working capital used for:		
Cash dividends	64,219	58,245
Additions to property, plant and equipment:		
Company owned property	40,392	34,239
Capitalized leased property	5,533	196
Reduction of long-term debt	77,315	36,157
Reduction of capital lease obligations	5,385	2,445
Purchase of common treasury shares	152,255	31,045
Retirement of preferred stock	6,266	2,112
Conversion of preferred stock	1,921	3,432
Other, net	—	1,814
	353,286	169,685
Acquisition (less working capital of $110,731 in 1987):		
Properties	—	53,719
Long-term debt	—	(43,514)
Excess of cost over fair value of net assets acquired	—	35,049
Other, net noncurrent assets	—	17,091
Net noncurrent assets	—	62,345
Change in net noncurrent assets of discontinued operations held for sale	(4,956)	1,354
	348,330	233,384
Increase (decrease) in working capital	$ 57,529	$ (37,800)
Working capital increased (decreased) by:		
Cash and marketable securities	$ (49,285)	$ (63,793)
Receivables	45,595	55,939
Inventories	81,399	81,986
Prepaid expenses and other current assets	8,680	1,651
Change in net current assets of discontinued operations held for sale	8,350	(4,514)
Notes payable	(1,677)	(65,322)
Current maturities	2,870	(2,350)
Accounts payable and accrued expenses	(38,560)	(30,369)
Income taxes	157	(11,028)
	$ 57,529	$ (37,800)

See accompanying notes to consolidated financial statements.

Consolidated Statement of Shareholders' Equity

(Dollars in thousands except per share data)

	Preferred Stock		Common Stock		Capital	Retained	
	Series D	**Series E**	**Issued**	**Treasury**	**Surplus**	**Earnings**	**Total**
Balance February 28, 1986	$ 66,027	$ —	$163,765	$ (81,739)	$ 104,205	$ 1,027,895	$ 1,280,153
Net earnings						125,774	125,774
Cash dividends:							
Preferred stock						(4,972)	(4,972)
Common stock—$1.57						(44,867)	(44,867)
By pooled company						(8,406)	(8,406)
Retirement of capital stock:							
Preferred—8,000 shares	(800)				(1,312)		(2,112)
Common—502,350 shares			(1,884)	15,354	(13,470)		—
Conversion of preferred stock:							
Series D—34,327 shares	(3,432)		556		2,874		(2)
Issuance of common stock:							
Options—193,610 shares			711	171	3,674		4,556
ESOP—20,126 shares				784	(6)		778
Restricted stock—132,045 shares			495		2,281		2,776
Purchase of 868,550 shares				(31,045)			(31,045)
Foreign currency translations						1,219	1,219
Conform pooled company						2,363	2,363
Balance February 28, 1987	61,795	—	163,643	(96,475)	98,246	1,099,006	1,326,215
Net earnings						145,003	145,003
Cash dividends:							
Preferred stock						(4,621)	(4,621)
Common stock—$1.60						(57,983)	(57,983)
By pooled company						(1,615)	(1,615)
Retirement of capital stock:							
Preferred—27,605 shares	(2,761)				(3,505)		(6,266)
Common—2,457,728 shares			(9,216)	63,315	(54,099)		—
Conversion of preferred stock:							
Series D—19,208 shares	(1,921)		311		1,609		(1)
Issuance of common stock:							
Options—93,321 shares			350	48	2,288		2,686
Purchase of 4,166,582 shares				(152,255)			(152,255)
Foreign currency translations						174	174
Balance February 29, 1988	57,113	—	155,088	(185,367)	44,539	1,179,964	1,251,337
Net earnings						70,150	70,150
Cash dividends:							
Preferred stock						(1,944)	(1,944)
Common stock—$0.86						(31,086)	(31,086)
Common stock rights—$0.025						(875)	(875)
Special cash—$38.60						(1,422,257)	(1,422,257)
Securities dividends:							
Debentures—$21.66						(789,657)	(789,657)
Preferred stock—$5.79		3,321			210,160	(213,481)	—
Retirement of capital stock:							
Common—3,900,549 shares			(14,627)	150,552	(135,925)		—
Conversion of preferred stock:							
Series D—552,030 shares	(55,203)		11,388		43,808		(7)
Issuance of common stock:							
Options—564,820 shares			2,118		15,735		17,853
Restricted stock—299,011 shares			1,121		1,020		2,141
Purchase of 2,220,550 shares				(102,341)			(102,341)
Foreign currency translations						936	936
Balance February 25, 1989	$ 1,910	$3,321	$155,088	$(137,156)	$ 179,337	$(1,208,250)	$(1,005,750)

See accompanying notes to consolidated financial statements.

1. SIGNIFICANT ACCOUNTING POLICIES

The Company and its subsidiaries follow generally accepted accounting principles to present fairly their consolidated financial position, results of operations, cash flows, and changes in financial position. The major accounting policies of the company are set forth below.

Principles of Consolidation — The consolidated financial statements include the accounts of the company and all its subsidiaries, the majority of which are wholly owned. All material intercompany transactions have been eliminated in consolidation.

Fiscal Year — The company changed its fiscal year to end on the last Saturday in February, effective with the current year. The company's fiscal year ended on the last day of February for fiscal years 1988 and 1987.

Statement of Cash Flows — In November 1987, the Financial Accounting Standards Board issued Statement No. 95 "Statement of Cash Flows." The company has adopted the provisions of Statement No. 95 in fiscal 1989 and has presented a statement of cash flows instead of a statement of changes in financial position. The company has elected not to restate the statement of changes in financial position presented for the fiscal years 1988 and 1987.

Two-for-One Stock Split — A two-for-one common stock split was effected July 23, 1986, and the number of shares and per share amounts included in the consolidated financial statements and notes thereto were restated to retroactively reflect the stock split.

Marketable Securities — Marketable equity securities (common and preferred stocks) are stated at the lower of cost or market. Aggregate net unrealized losses are included in results of operations if related to current assets and in shareholders' equity if related to noncurrent assets. Other marketable securities are stated at cost, which approximates market value, unless there is an indication of permanent impairment of value, in which case the adjustment to market value is included in results of operations. The cost of marketable securities sold is determined on the specific identification method. For purposes of the statement of cash flows, the company considers all short-term investments with a maturity at date of purchase of three months or less to be cash equivalents.

Inventories — Inventories are stated at the lower of cost (first-in, first-out) or market, except for certain footwear manufacturing inventories which are valued on the "last-in, first-out" method of inventory valuation.

Property, Plant and Equipment — Property, plant and equipment, including facilities and equipment leased under capital leases, are stated at cost. Expenditures for improvements are capitalized, while normal repairs and maintenance are expensed as incurred. When properties are retired or otherwise disposed of, the related cost and accumulated depreciation or amortization are removed from the accounts and gains or losses on the dispositions are reflected in results of operations. For financial reporting purposes, the company utilizes both accelerated and straight-line methods of computing depreciation and amortization. Such expense is computed based on the estimated useful lives of the respective assets or term of lease, if less, which generally range from 15 to 40 years for buildings and improvements, and from 3 to 20 years for machinery and equipment. Approximately 70% of depreciation and amortization expense was computed using the straight-line method in each fiscal year presented.

Excess of Cost Over Fair Value of Net Assets Acquired — The excess of cost over fair value of net assets of companies acquired is included in other assets and is generally amortized on a straight-line basis, over periods ranging from 25 to 40 years.

Income Taxes — Deferred income taxes are provided on transactions which are reported for financial reporting purposes in different periods than for income tax purposes. It is the company's intent that the undistributed earnings of its subsidiaries will either be reinvested in the subsidiaries or distributed tax-free to the parent company. Generally, no provision has been made for income taxes on such undistributed earnings. The Financial Accounting Standards Board issued Financial Accounting Standard No. 96 — Accounting for Income Taxes, in December 1987. This standard requires an asset and liability approach to accounting for deferred income taxes. Initial adoption of this pronouncement may be done on either a prospective or retroactive basis, with a required implementation date beginning with the company's first quarter of fiscal 1991. Management is of the opinion that the adoption of these new accounting regulations will not have a material impact on the consolidated financial statements.

2. BUSINESS COMBINATIONS

During fiscal 1988, the company acquired all the outstanding stock of The Lane Company, Incorporated in exchange for 11,616,023 shares of the company's common stock. Prior to the exchange of shares, the company acquired 334,900 common shares of The Lane Company, Incorporated in fiscal 1987 for cash of $15,140. This transaction was accounted for as a pooling of interests; and, accordingly, the accounts of this company have been included in the accompanying consolidated financial statements for fiscal 1988 and fiscal 1987. Prior to restatement for this business combination, consolidated net sales and net earnings, from continuing operations, of the company for fiscal 1987 were $1,297,755 and $56,353, respectively. The Lane Company, Incorporated reported net sales of $333,163 and net earnings of $27,345 for their fiscal year ended January 3, 1987. Retained earnings, as of February 28, 1987, have been adjusted for the pooled company's operations for the months of January and February 1987. This acquisition is included in the Furniture and Home Furnishings Segment of the company.

On September 8, 1986, the company acquired all the outstanding stock of Converse Inc. The acquisition price of $143,717, including capitalized expenses, was paid in cash. The transaction was accounted for as a purchase and accordingly, Converse's operations have been included in the consolidated financial statements and in the Footwear Manufacturing and Retailing Segment of the company from the date of acquisition. The total acquisition cost exceeded the fair value of the net assets acquired by $28,781, and the excess has been allocated to goodwill. Also, in fiscal 1987, the company made three smaller acquisitions for cash payments totaling $29,359.

3. DISCONTINUED OPERATIONS

During the second quarter of fiscal 1989, the company announced its intent to offer for sale the Apparel Manufacturing Group, and in the fourth quarter offered for sale the General Retail Merchandising Group. In accordance with Accounting Principles Board Opinion No. 30, the financial results for the groups are reported as "Discontinued Operations" and results from prior periods have been restated. Condensed results of the discontinued operations were as follows:

	1989	1988	1987
Net sales	**$1,265,789**	$1,345,449	$1,315,984
Pretax earnings	**67,543**	54,723	82,906
Income taxes	**27,047**	23,154	40,616
Net earnings	**40,496**	31,569	42,290
Gain on disposal (net of income tax of $28,000)	**33,936**	—	—
Accounts receivable, net	**$ 122,737**	$ 176,603	$ 182,297
Inventory	**205,531**	290,901	301,113
Other current assets	**17,615**	19,265	17,104
Total current assets	**345,883**	486,769	500,514
Current liabilities	**97,522**	104,027	126,122
Net current assets	**$ 248,361**	$ 382,742	$ 374,392
Property, plant and equipment, net	**$ 139,531**	$ 162,261	$ 172,568
Other assets	**4,061**	27,799	28,746
Total	**143,592**	190,060	201,314
Long-term liabilities	**45,581**	51,158	57,456
Net other assets	**$ 98,011**	$ 138,902	$ 143,858

On December 29, 1988, the company completed the sale of its Londontown Corporation subsidiary for $178,000 in cash. The gain recognized in the sale was reflected in the Statement of Earnings. Also included in the gain on disposal for fiscal 1989 is the write-off of $20,564 in goodwill, which was nondeductible for income tax purposes, associated mainly with the Apparel Group.

(Dollars in thousands except per share data)

On February 24, 1989, the company sold the assets, net of liabilities, of The Biltwell Company for approximately $42,000 in cash.

Management anticipates that disposal of the remaining companies in the Apparel and Retail Groups will be completed in cash sales during fiscal 1990.

4. INVENTORIES

Inventories are summarized as follows:

	1989	1988	1987
Retail merchandise	**$129,723**	$137,499	$130,444
Finished products	**216,739**	225,337	172,719
Work-in-process	**52,167**	51,653	44,333
Raw materials	**92,338**	99,704	85,298
	$490,967	$514,193	$432,794

All of the major categories of inventory, except retail merchandise, include certain items valued on the "last-in, first-out" method. Had the "first-in, first-out" method been applied to all inventories, they would have been stated at approximately $511,325, $537,146 and $461,621 at fiscal years 1989, 1988 and 1987, respectively.

5. LINES OF CREDIT

The company's eight-year domestic revolving credit agreement enabling it to borrow up to $150,000 from several U.S. banks and its five-year credit agreement enabling it to borrow up to $50,000 in Euro-Dollar loans from a group of foreign banks under various borrowing options based on Euro-Dollar interest rates was replaced in November, 1988 by the Secured Credit Agreement included in long-term debt.

Average short-term borrowings outstanding during fiscal 1989, 1988 and 1987 were $208,000, $123,000, and $57,000, respectively, with a weighted average interest rate thereon of 7.8%, 7.1% and 6.1%, respectively. Maximum short-term borrowings at any month-end were $290,500, $172,500 and $141,500 in fiscal years 1989, 1988 and 1987, respectively.

6. LONG-TERM DEBT

Long-term debt consisted of the following:

	1989	1988	1987
Secured credit agreement	**$1,424,847**	$ —	$ —
7.95% to 8.875% promissory notes due 1991 to 1993	**200,000**	200,000	—
14.25% promissory notes	**—**	—	75,000
5% to 12% industrial revenue bonds payable in varying amounts through 2011	**41,352**	41,798	44,631
Other debt at 6.5% to 8.75% interest rates, payable in varying amounts through 2006	**11,065**	17,537	20,740
	1,677,264	259,335	140,371
Less current maturities	**507,335**	2,008	5,729
	$1,169,929	$257,327	$134,642

During the third quarter of fiscal 1989, the company entered into the Secured Credit Agreement with a group of banks. Borrowings under the agreement were utilized to fund the special cash dividend payments declared by the Board of Directors as part of the company's restructuring plan.

The outstanding borrowings under the Secured Credit Agreement bear interest at the company's option at either the prime rate plus 1½% or adjusted LIBOR plus 2½%. Of the borrowings outstanding at February 25, 1989, $287,500 was issued under the LIBOR option and bears interest at 13.07%. The interest rate for the remainder of the borrowings under this agreement was 13% at February 25, 1989.

Under the Secured Credit Agreement, the company is required to satisfy certain financial tests. At February 25, 1989, the company was not in compliance with the coverage ratio and the interest coverage ratio covenants. The bank syndicate has granted temporary waivers in this regard.

The loans available under the Secured Credit Agreement consist of a $1,150,000 Asset Sale Bridge Facility, a $265,000 Term Loan Mortgage Bridge Facility, a $250,000 Borrowing Base Facility and a $250,000 Seasonal Working Capital Facility providing for letters of credit as well as for loans. On November 29, 1988, the company borrowed $1,655,000 to pay the cash portions of the special dividend and to refinance existing debt.

The $999,847 amount outstanding at fiscal year end under the Asset Sale Bridge Facility must be reduced to $500,000 by August 7, 1989, and the remaining balance outstanding thereunder is payable by May 7, 1990. The Secured Credit Agreement requires the company to sell stock or assets of existing business units, other than the core companies of Converse, Florsheim, Broyhill and Lane, sufficient to fund these mandatory reductions.

The Term Loan Mortgage Bridge Facility must be reduced by $75,000 by May 7, 1990, and by 1/17 of the difference between $75,000 and the $225,000 outstanding on December 31, 1988, on each November 7, February 7, May 7 and August 7 from November 7, 1989 to November 7, 1993. The Secured Credit Agreement requires the company and its subsidiaries to incur debt secured by mortgages on real property in an amount sufficient to fund the $75,000 reduction of the Term Loan Mortgage Bridge Facility required by May 7, 1990. The Term Loan Mortgage Bridge Facility matures on November 7, 1993. At fiscal year end, $230,000 was outstanding under this facility.

The Borrowing Base Facility matures on November 7, 1993, and the Seasonal Working Capital Facility matures on November 7, 1991. The company has borrowings outstanding at February 25, 1989 of $175,000 under the Borrowing Base Facility and $20,000 under the Seasonal Working Capital Facility. Aggregate Loans outstanding under these Facilities may not exceed the "Borrowing Base," as defined in the Secured Credit Agreement. The Borrowing Base is computed by reference to the amount of inventory and accounts receivable of the company and certain subsidiaries, and will be reduced by $40,000 on August 7, 1989, and by a further $20,000 on the earlier of May 7, 1990 and the date no loans remain outstanding under the Asset Sale Bridge Facility.

On the earlier of May 7, 1990 and the date the company sells its Apparel Group, total availability under the Seasonal Working Capital Facility will be reduced from $250,000 to $200,000 and the portion of the Seasonal Working Capital Facility reserved for issuance of letters of credit (each of which must expire by November 7, 1991) will be reduced from $100,000 to $75,000. No more than $30,000 in stand-by letters of credit, or $100,000 in trade letters of credit ($75,000 after the earlier of May 7, 1990 and the date the company sells its Apparel Group), may be outstanding at any time. In addition, the aggregate principal amount of loans outstanding under the Seasonal Working Capital Facility may not exceed (i) $175,000 (reduced to $150,000 on the earlier of May 7, 1990 and the date the company sells its Apparel Group) at any time, or (ii) $75,000 for a period of at least 30 consecutive days during the period from January 1 through February 28 of each year, commencing January 1, 1989.

The borrowings and other extensions of credit under the Secured Credit Agreement are unconditionally guaranteed by each wholly-owned active domestic subsidiary of the company, such guarantees being limited to the maximum amount which will not result in a violation of creditors' rights under relevant principles of law. Such borrowings and the guarantees thereof are secured by (i) mortgages or deeds of trust on certain real property owned by the company and its subsidiaries, (ii) patent and trademark security agreements covering patents and trademarks owned by the company and its subsidiaries, (iii) security interests in inventory, accounts receivable, equipment and other personal property of the company and its subsidiaries, and (iv) pledges of the

(Dollars in thousands except per share data)

stock of active domestic subsidiaries of the company. Under the Secured Credit Agreement, the banks also have the right to require (to the extent permitted under the then-existing agreements) that real or personal property of the company or any active domestic subsidiary not at the time subject to a lien or security interest in favor of the banks be subjected to such a lien and that active domestic subsidiaries the stock of which is not at the time pledged to the banks be so pledged.

The company is required to pay a commitment fee of ½ of 1% per annum on the average daily amount of the commitments of the banks, less the average daily amount of loans outstanding, payable quarterly in arrears until such commitments are terminated. The principal amount of the commitment, upon which the commitment fee is calculated, was $1,915,000. The company will also pay an annual agency fee of $400 and certain other fees and expenses in connection with the Secured Credit Agreement.

In addition, a fee of 2½% per annum on the daily average available amount under each letter of credit is payable upon issue for the account of the lenders ratably; a further fee of not more than ¼ of 1% per annum on the daily average available amount under each letter of credit and a customary administrative charge for issuance of the letter of credit are each payable to the relevant issuing bank. Letter of credit fees will be payable quarterly in arrears.

During the fourth quarter of fiscal 1988, the company issued $200,000 of intermediate term promissory notes with various interest rates and maturity dates. A January 15, 1988 promissory note in the amount of $125,000 with an interest rate of 8.875% matures on January 15, 1993. Three promissory notes in the amount of $25,000 each were issued on February 5, 1988, February 25, 1988 and February 16, 1988, with interest rates of 7.95%, 8.30% and 8.45%, and with maturity dates of February 5, 1991, February 25, 1992, and February 16, 1993, respectively. The $125,000 promissory note was issued at a discount of $938 and the discount and the costs relating to the issuance of the notes are being amortized over the respective lives of the notes as a charge to interest expense.

Maturities of long-term debt are $507,335, $531,689, $46,458, $153,364 and $406,377 for fiscal years 1990 through 1994, respectively.

The 14.25% promissory notes were redeemed on February 15, 1988, at the principal amount, without premium.

Included in other assets is $43,457 in unamortized deferred debt costs which are being amortized over the life of the debt instrument. The majority of these deferred costs relate to the debt incurred in the restructuring.

7. DEBENTURES

The debentures were issued as part of the special dividends declared by the Board of Directors in fiscal 1989 in the restructuring plan and consist of the following, by class of debenture:

	1989
13.75% Senior Subordinated Debentures, net of unamortized original issue discount of $7,967, due December 15, 2000	**$396,403**
14.0% Subordinated Discounted Debentures, net of unamortized original issue discount of $158,061, due December 15, 2003	**228,237**
14.5% Payment-in-Kind Debentures, net of unamortized original issue discount of $22,604, due December 15, 2003	**184,017**
	$808,657

The Senior Subordinated Debentures mature on December 15, 2000, pay interest semiannually at the rate of 13.75% and require three annual sinking fund payments of 25% of the principal amount commencing on December 15, 1997 to retire 75% of the debentures prior to final maturity. On or after December 15, 1992, the debentures may be redeemed at the company's option at 108.75% of face value, decreasing to 100% in 1997. The debentures are subordinated in right of payment to all senior debt of the company.

The Subordinated Discount Debentures mature on December 15, 2003, and require three annual sinking fund payments of 25% of the principal amount commencing on December 15, 2000 to retire 75% of the debentures prior to final maturity. Interest on the debentures will accrue commencing December 15, 1991 at the rate of 14.0%, and will be payable semiannually with the first interest payment on June 15, 1992. On or after December 15, 1995 the debentures may be redeemed at the company's option at 108.75% of face value, decreasing to 100% in 2000. The debentures are subordinated in right of payment to all senior debt, including the Senior Subordinated Debentures of the company.

The Junior Pay-in-Kind Subordinated Debentures mature on December 15, 2003. Interest is payable semiannually at the rate of 14.5% commencing on June 15, 1989, and at the option of the company, may be paid in additional debentures until December 15, 1993. On or after December 15, 1995, the debentures may be redeemed at the company's option at 109.25% of face value, decreasing to 100% in 2000. The debentures are subordinated in right of payment to all senior debt, including the Senior Subordinated Debentures and the Discount Debentures of the company.

8. OBLIGATIONS UNDER CAPITAL LEASES

The amount capitalized under capital leases is the lesser of the present value of the minimum lease payments or the fair value of the leased properties at the beginning of the respective lease terms. Generally, interest rates applicable to capital leases range between 8.6% and 16.7% for leased facilities and between 5.5% and 10.7% for leased equipment. Obligations under capital leases amounted to $10,877, $11,672 and $10,673 at fiscal years ended 1989, 1988 and 1987, respectively. Maturities of these obligations are $2,626, $2,222, $1,900, $976 and $415 for fiscal years 1990 through 1994, respectively.

9. PREFERRED STOCK

The company's preferred stock consisted of:

Series D — At fiscal years ended 1989, 1988 and 1987, the outstanding Series D preferred stock consisted of 19,103, 571,133 and 617,946 shares, respectively, of $7.75 cumulative convertible with stated and involuntary liquidating value of $100.00 per share.

Each share of the Series D preferred stock is convertible into 91.0028 shares (4.3242 prior to the restructuring) of the company's common stock. The Series D preferred stock may be redeemed at the company's option at $104.75 per share in 1989, decreasing to $100.00 per share in 1994 and accumulated dividends.

Subsequent to February 25, 1989, the Board of Directors was required under Delaware corporation law to omit the March 15, 1989 quarterly dividend of $1.9375 per share on the Series D preferred stock. The dividend arrearage on the 14,610 shares outstanding at the record date was $28.

Series E — At fiscal year ended 1989, 3,320,702 shares of Series E preferred stock, including those represented by depositary receipts, were outstanding. The Series E pays quarterly dividends at an annual rate of 17.5%, and had a $100.00 per share initial aggregate liquidation preference. Payments commence on March 15, 1989, are payable in cash or prior to December 15, 1994, in Series E preferred stock, and if not paid in cash or stock, the aggregate liquidation preference increases 4.375% quarterly.

Each share of Series E preferred stock, including the shares represented by depositary receipts, may be redeemed at the company's option at 101% of the then Aggregate Liquidation Preference per share, plus accrued dividends, through December 15, 1994 and at 100% thereafter. The shares are exchangeable, at the company's option, on any dividend date after December 15, 1994 into Junior Subordinated Exchange Debentures, which would bear interest at the same rate as the Series E.

Each share of Series E, including the shares represented by depositary receipts, carried warrants to purchase 3.5 shares of common stock at $6.25 per share. At March 14, 1989 the warrants separated from the Series E and warrant certificates evidencing the right to purchase 11,622,457 shares of common stock were issued. The warrants become exercisable on July 1, 1989 and expire on March 15, 1992.

(Dollars in thousands except per share data)

10. COMMON STOCK

Shares of common stock were reserved for the following purposes at February 25, 1989:

	Number of Shares
Common stock options:	
Granted	4,146,834
Acquired companies options assumed	21,300
Available for grant	1,032,575
Restricted stock plan of acquired company	162,676
Conversion of Series D preferred stock	1,738,426
	7,101,811

Under the company's stock option plans, certain key employees may be granted incentive options, nonqualified options, stock appreciation rights, or combinations thereof. Nonqualified options and stock appreciation rights granted under the 1977 Plan may not be less than 85% of the fair market value (100% as to incentive options and related stock appreciation rights) of the common stock on the date of grant. Options and stock appreciation rights granted under the 1980 and 1985 Plans may not be less than 100% of the fair market value of the common stock on the date of grant. All options which have been granted, incentive or nonqualified, were at 100% of fair market value on the date of grant. Incentive options and nonqualified options expire ten years after the date of grant. At February 25, 1989, no appreciation rights have been granted. Options outstanding and the exercise prices thereon and shares available for grant, were adjusted in accordance with anti-dilution provisions of the plans subsequent to the record dates of the restructuring dividends.

At February 25, 1989, information regarding options granted but not exercised was as follows:

	Option Shares Outstanding	Dates of Grant	Price Range
1977 Plan	172,132	July 2, 1979 - March 10, 1987	$1.3468 - $3.00
1980 Plan	2,534,037	December 19, 1980 - July 30, 1987	$1.4217 - $3.5387
1982 Plan	21,300	November 3, 1986	$2.0183
1985 Plan	1,440,665	March 10, 1987 - July 30, 1987	$3.00 - $3.5387

Changes in options granted are summarized as follows:

	1989		1988		1987	
	Shares	**Average Price**	Shares	Average Price	Shares	Average Price
Beginning of year	**850,312**	**$32.30**	637,120	$27.17	800,756	$26.85
Assumed option of acquired companies	—	—	103,488	24.02	6,743	4.84
Restructuring dividends	**4,276,147**	—	—	—	—	—
Granted	—	—	284,250	42.94	—	—
Exercised	**(564,820)**	**25.31**	(93,321)	24.67	(142,479)	24.21
Cancelled	**(393,505)**	**5.79**	(81,225)	29.75	(27,900)	27.82
End of year	**4,168,134**	**$ 2.61**	850,312	$32.30	637,120	$27.17
Exercisable at end of year	**1,723,975**		383,181		283,197	

On January 23, 1989, the Board of Directors adopted, subject to shareholder approval, the 1989 Plan, under which nonqualified options to purchase 7,500,000 shares of common stock may be granted, of which, options to purchase 4,580,000 shares have been granted. All grants are at market value on the date of grant.

Under programs for purchasing the company's stock, 2,220,550 shares of common stock were repurchased during fiscal 1989 at a cost of $102,341. Beginning in fiscal 1988, common treasury shares are retired and restored to the status of authorized but unissued shares as new issue common shares are used for employee benefit plans and for the conversion of the company's preferred stock.

In fiscal 1986, the company declared a dividend of one Common Share Purchase Right for each then outstanding share of common stock. The rights were redeemed on July 21, 1988 for $875. On July 11, 1988 the company declared a dividend of one Common Share Purchase Right for each outstanding share of common stock, effective July 21, 1988. The rights will not be exercisable, or transferable apart from the common stock, until ten days after another person or group of persons acquires 15% or more of the common stock or commences, or announces its intention to commence, a tender or exchange offer for 15% or more of the common stock. Each right entitles its holder to buy one share of common stock at an exercise price of $160.00 (subject to adjustment pursuant to the anti-dilution provisions of the plan). In certain circumstances, the rights will entitle their holders to purchase larger amounts of common stock or stock in an acquiring company. In addition to the shares reserved above, an additional 48,458,658 shares have been reserved under this plan.

11. INCOME TAXES

Income tax expenses were comprised of the following:

	1989	1988	1987
Current:			
Federal	**$14,814**	$69,999	$53,799
State and local	**9,403**	13,262	9,919
Foreign	**2,598**	1,716	2,415
	26,815	84,977	66,133
Deferred	**(6,838)**	326	5,188
	$19,977	$85,303	$71,321
ESOP and jobs tax credits	**$ –**	$ 140	$ 741

The following table reconciles the differences between the Federal corporate statutory rate and the company's effective income tax rate:

	1989	1988	1987
Federal corporate statutory rate	**34.0%**	38.0%	46.0%
State and local income taxes, net of Federal tax benefit	**40.0**	4.5	3.3
ESOP, investment and jobs tax credits	**–**	(0.1)	(0.5)
Foreign taxes, including foreign currency translation effects	**19.2**	0.4	0.2
Nondeductible restructuring costs	**30.3**	–	–
Other	**3.8**	0.1	(2.9)
Effective income tax rate	**127.3%**	42.9%	46.1%

(Dollars in thousands except per share data)

Certain items are recognized for income tax purposes in years other than those in which they are reported in the consolidated financial statements. Future income tax benefits and deferred credits at the end of each fiscal year are included in the accompanying consolidated balance sheet, as follows:

	1989	1988	1987
Prepaid expenses and other current assets	**$ 23,584**	$ 7,020	$ 3,615
Other long-term liabilities	**(33,386)**	(29,777)	(26,103)
	$ (9,802)	$(22,757)	$(22,488)

The Federal income tax returns of the company and its major subsidiaries have been examined through fiscal year ended February 28, 1986.

12. EMPLOYEE BENEFITS

The company and its subsidiaries sponsor or contribute to retirement plans covering substantially all employees. The total cost of all plans for fiscal years 1989, 1988 and 1987 was $8,695, $10,058 and $11,151, respectively.

Company Sponsored Defined Benefit Plans – In fiscal 1988 the company adopted Financial Accounting Standards (FAS) Statement No. 87 – Employers' Accounting for Pensions, which superseded all previous standards of pension accounting.

Annual cost for domestic defined benefit plans under FAS 87 is determined using the Projected Unit Credit actuarial method. Prior service cost is amortized on a straight-line basis over the average remaining service period of employees expected to receive benefits.

It is the company's practice to fund pension costs to the extent that such costs are tax deductible. Funding decisions made in fiscal 1989 contributed towards the deferred or prepaid pension cost in U.S. plans. The assets of the various plans include corporate equities, government securities, corporate debt securities, income producing real estate, and insurance contracts.

The tables provide information on the status of the U.S., company sponsored, defined benefit plans.

The funded status at fiscal year end 1989 and 1988 was as follows:

	1989		1988	
	Plans in which		Plans in which	
	Assets Exceed Accumulated Benefits	**Accumulated Benefits Exceed Assets**	Assets Exceed Accumulated Benefits	Accumulated Benefits Exceed Assets
Actuarial present value of benefit obligations:				
Vested benefit obligation	**$177,422**	**$ 2,364**	$155,423	$11,339
Accumulated benefit obligation	**$184,918**	**$ 3,171**	$163,194	$11,974
Projected benefit obligation	**$211,262**	**$ 3,508**	$191,031	$13,657
Plan assets at fair value	**257,865**	**1,207**	236,988	9,939
Projected benefit obligation less than (in excess of) plan assets	**46,603**	**(2,301)**	45,957	(3,718)
Unrecognized net (gain) loss	**(19,047)**	**25**	(18,305)	(1,967)
Unrecognized prior service cost	**203**	**–**	–	–
Unrecognized net (asset) obligation at year end	**(23,233)**	**978**	(26,820)	3,198
Prepaid (accrued) pension cost recognized in the consolidated balance sheet	**$ 4,526**	**$(1,298)**	$ 832	$ (2,487)

Net periodic pension cost for the fiscal years ended 1989 and 1988 include the following components:

	1989	1988
Service cost — benefits earned during the period	**$ 4,624**	$ 5,382
Interest cost on the projected benefit obligation	**14,184**	13,192
Actual return on plan assets	**(15,543)**	6,385
Net amortization and deferral	**437**	(20,663)
Net periodic pension cost	**$ 3,702**	$ 4,296

The company recognized $2,388 of curtailment gain in fiscal 1989 associated with discontinued operations.

Employees are covered primarily by noncontributory plans, funded by company contributions to trust funds, which are held for the sole benefit of employees. Monthly retirement benefits generally are based upon service, pay, or both, with employees generally becoming vested upon completion of 10 years of service.

The expected long-term rate of return on plan assets was 8.0%-8.5% in fiscal 1989. Measurement of the fiscal 1989 projected benefit obligation was based on a 9.25% discount rate and a 5.5% long-term rate of compensation increase.

Other Retirement Plans and Benefits — In addition to defined benefit plans, the company makes contributions to various defined contribution, union negotiated, and foreign plans. The cost of these plans is included in the total cost for all plans reflected above.

The company has a Savings Plan for Employees of INTERCO INCORPORATED and Affiliates and an INTERCO INCORPORATED Employee Stock Ownership Plan (ESOP). The total cost of these plans for fiscal years 1989, 1988 and 1987 was $548, $474 and $403, net of taxes of $411, $359 and $708, respectively.

The company provides certain health care and life insurance benefits for certain employees who reach retirement age. Retiree health and life insurance benefits are provided through insurance companies. Post-retirement health care and life insurance expense for fiscal years 1989, 1988 and 1987 was $1,306, $1,195, and $1,318, respectively.

13. LEASE COMMITMENTS

Substantially all of the company's retail outlets and certain other real properties and equipment are operated under lease agreements expiring at various dates through the year 2022. Leases covering retail outlets and equipment generally require, in addition to stated minimums, contingent rentals based on retail sales and equipment usage. Generally, the leases provide for renewal for various periods at stipulated rates.

Assets recorded under capital leases were as follows:

	1989	1988	1987
Land	**$ 321**	$ 390	$ 324
Buildings	**11,104**	12,720	13,347
Machinery and equipment	**9,844**	10,096	5,795
	21,269	23,206	19,466
Accumulated depreciation	**10,523**	11,396	8,872
	$10,746	$11,810	$10,594

(Dollars in thousands except per share data)

Future minimum lease payments under capital leases reduced by minimum rentals from subleases of $3,092 at February 25, 1989 aggregate $15,702, of which $10,877 is included in obligations under capital leases and current maturities, $4,476 represents interest, and the balance represents other costs of the leases including taxes, insurance and maintenance. Annual payments under capital leases are $3,675, $3,033, $2,504, $1,420 and $757 for fiscal years 1990 through 1994, respectively.

Total rent expense was as follows:

	1989	1988	1987
Basic rentals under operating leases	**$33,323**	$27,506	$29,053
Contingent rentals, operating and capital leases	**31,849**	28,230	29,809
	65,172	55,736	58,862
Less sublease rentals	**1,729**	568	679
	$63,443	$55,168	$58,183

Included in rent expense above is the cost of services provided by lessors of leased retail departments, estimated to aggregate $15,100, $17,800, and $18,500 in fiscal years 1989, 1988 and 1987, respectively.

Future minimum lease payments under operating leases, reduced by minimum rentals from subleases of $8,389, at February 25, 1989, aggregate $149,876. Annual payments under operating leases are $29,981, $27,644, $22,200, $16,972 and $12,985 for fiscal years 1990 through 1994, respectively.

The company has also guaranteed leases of the discontinued operations which at February 25, 1989 aggregated approximately $112,474, based on minimum rentals.

14. LITIGATION

In fiscal 1989, certain shareholder actions were filed against the company and its directors in the United States District Court for the Southern District of New York and the Delaware Court of Chancery. These actions allege, among other things, that the directors of the company violated the federal securities laws and breached their fiduciary duties to the company's shareholders in connection with Cardinal Acquisition Corp.'s tender offer for the company's stock. The suits seek damages and other remedies. The company believes that these shareholder suits are without merit and intends to defend them vigorously. Although the amount of any ultimate liability cannot be determined, in the opinion of management, after consultation with the company's legal counsel, these claims when resolved will not have a material adverse effect on the consolidated financial condition of the company and its subsidiaries.

The company is or may become a defendant in a number of pending or threatened legal proceedings in the ordinary course of business. In the opinion of management, the ultimate liability, if any, of the company from all such proceedings will not have a material adverse effect upon the consolidated financial condition of the company and its subsidiaries.

15. EARNINGS PER SHARE

Earnings per share are based on the weighted average number of shares of common stock and common stock equivalents outstanding during the year, plus those common shares which would have been issued if conversion of all preferred stock had taken place at the beginning of each year or since date of issuance. Stock options, the exercise of which would result in dilution of earnings per share, are considered common stock equivalents. Net earnings for these computations are reduced by the preferred stock dividend requirements.

16. BUSINESS SEGMENT INFORMATION

The company's two business segments are Footwear Manufacturing and Retailing, and Furniture and Home Furnishings. Specific information, on an unaudited basis, relating to the operating companies and their products, which comprise each segment, is included on the inside front cover. Summarized financial information by business segment is as follows:

	1989	1988	1987
Net sales to unaffiliated customers:			
Footwear	**$ 915,447**	$ 890,411	$ 663,521
Furniture	**1,096,515**	1,105,563	967,397
Total	**$2,011,962**	$1,995,974	$1,630,918
Operating earnings:			
Footwear	**$ 45,565**	$ 92,204	$ 52,136
Furniture	**131,731**	149,090	123,766
	177,296	241,294	175,902
Corporate and restructuring expenses and interest cost	**(161,601)**	(42,557)	(21,097)
Earnings from continuing operations before income taxes	**$ 15,695**	$ 198,737	$ 154,805
Identifiable assets at year end:			
Footwear	**$ 595,977**	$ 595,861	$ 497,706
Furniture	**715,636**	688,853	640,106
	1,311,613	1,284,714	1,137,812
Discontinued operations	**346,372**	521,644	518,250
Corporate assets	**117,317**	24,042	85,747
Total	**$1,775,302**	$1,830,400	$1,741,809
Depreciation expense:			
Footwear	**$ 13,694**	$ 13,107	$ 10,638
Furniture	**24,964**	26,208	21,675
Capital expenditures:			
Footwear	**$ 14,020**	$ 9,236	$ 7,486
Furniture	**38,635**	36,188	24,720

Operating earnings of the business segment include its sales less all operating expenses. Minority interests in certain subsidiaries are immaterial and have been included in corporate expenses and interest cost. Substantially all of the company's sales are made to unaffiliated customers. No customer accounted for 10% or more of consolidated sales. Foreign operations are not material.

Identifiable assets are those assets used by each segment in its operations. Corporate assets consist primarily of cash and marketable securities. Realized gains (losses) on the sale of marketable securities netted against corporate expenses and interest cost amounted to $4,998, $(181) and $13 for fiscal years 1989, 1988 and 1987, respectively.

(Dollars in thousands except per share data)

17. QUARTERLY FINANCIAL INFORMATION (UNAUDITED)

Following is a summary of unaudited quarterly information for each of the years in the three year period ended February 25, 1989.

	First	Second	Third	Fourth
Net Sales:				
1989	$490,062	$491,335	$547,449	$483,116
1988	472,944	474,248	548,605	500,177
1987	363,611	335,267	475,538	456,502
Gross Profit:				
1989	$173,989	$164,052	$181,551	$156,692
1988	168,626	167,497	188,173	182,930
1987	128,391	121,717	164,077	165,623
Net Earnings (Loss) From Continuing Operations:				
1989	$ 23,756	$ 18,689	$ (4,576)	$ (42,151)
1988	19,332	24,896	36,762	32,444
1987	15,257	14,393	22,113	31,721
Net Earnings From Discontinued Operations:				
1989	$ 6,933	$ 16,192	$ 15,082	$ 36,225
1988	7,182	13,533	6,687	4,167
1987	5,247	14,865	13,528	8,650
Total Net Earnings (Loss):				
1989	$ 30,689	$ 34,881	$ 10,506	$ (5,926)
1988	26,514	38,429	43,449	36,611
1987	20,504	29,258	35,641	40,371
Earnings (Loss) Per Share From Continuing Operations:				
1989	$ 0.62	$ 0.50	$ (0.11)	$ (1.43)
1988	0.45	0.58	0.89	0.82
1987	0.35	0.33	0.51	0.74
Total Earnings (Loss) Per Share:				
1989	$ 0.80	$ 0.93	$ 0.29	$ (0.49)
1988	0.62	0.90	1.05	0.93
1987	0.47	0.68	0.82	0.94
Common Dividends Paid Per Share:				
1989	$ 0.430	$ 0.455	$ 38.600	$ 27.446
1988	0.400	0.400	0.400	0.400
1987	0.385	0.385	0.400	0.400
Common Stock Price Range (High-Low):				
1989	$ 46-40	$ 73-41	$ 73-29	$ 32-2⅝
1988	46-38	54-40	53-30	42-30
1987	45-37	48-39	47-38	45-37

The closing market price of INTERCO's Common and Series E Preferred Stock at fiscal year end 1989 was $3.50 and $71.50 per share, respectively.

During the fourth quarter of fiscal 1989, gross profit margins were 32.4% as compared to 36.6% in fiscal 1988 and 36.3% in fiscal 1987. Margins in fiscal 1989 were adversely impacted by the results of the Footwear Manufacturing and Retailing Group due to promotional costs and unfavorable manufacturing variances resulting from the sales decline in canvas footwear, and manufacturing start-up costs within the athletic footwear segment.

Independent Auditors' Report

The Board of Directors and Shareholders
INTERCO INCORPORATED

We have audited the accompanying consolidated balance sheets of INTERCO INCORPORATED and subsidiaries as of February 25, 1989, February 29, 1988 and February 28, 1987, and the related consolidated statements of earnings and changes in shareholders' equity for each of the years in the three year period ended February 25, 1989, the consolidated statement of cash flows for the year ended February 25, 1989, and the consolidated statements of changes in financial position for the years ended February 29, 1988 and February 28, 1987. These consolidated financial statements are the responsibility of the company's management. Our responsibility is to express an opinion on these consolidated financial statements based on our audits.

We conducted our audits in accordance with generally accepted auditing standards. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free of material misstatement. An audit includes examining, on a test basis, evidence supporting the amounts and disclosures in the financial statements. An audit also includes assessing the accounting principles used and significant estimates made by management, as well as evaluating the overall financial statement presentation. We believe that our audits provide a reasonable basis for our opinion.

In our opinion, the consolidated financial statements referred to above present fairly, in all material respects, the financial position of INTERCO INCORPORATED and subsidiaries at February 25, 1989, February 29, 1988 and February 28, 1987, the results of their operations for each of the years in the three year period ended February 25, 1989, their cash flows for the year ended February 25, 1989, and their changes in financial position for the years ended February 29, 1988 and February 28, 1987 in conformity with generally accepted accounting principles.

As discussed in Note 1 to the consolidated financial statements, the company adopted Statement of Financial Accounting Standards No. 95 "Statement of Cash Flows", in 1989.

Peat Marwick Main & Co.

St. Louis, Missouri
April 10, 1989

Five Year Consolidated Financial Review

(Dollars in thousands except per share data)

Years Ended	1989	1988	1987	1986	1985
For The Year					
Summary of operations:					
Net sales	**$ 2,011,962**	$1,995,974	$1,630,918	$1,462,766	$1,422,280
Cost of sales	**1,335,678**	1,288,748	1,051,110	943,970	982,536
Interest expense	**141,735**	29,188	23,061	20,888	21,120
Earnings from continuing operations before income taxes	**15,695**	198,737	154,805	136,549	92,793
As a percent of sales	**0.8%**	10.0%	9.5%	9.3%	6.5%
Income taxes	**19,977**	85,303	71,321	65,040	45,238
Net earnings (loss) from continuing operations	**(4,282)**	113,434	83,484	71,509	47,555
As a percent of sales	**(0.2%)**	5.7%	5.1%	4.9%	3.3%
Discontinued operations	**74,432**	31,569	42,290	48,340	47,938
Net earnings applicable to common stock	**58,366**	145,003	125,774	119,853	95,502
Per share of common stock:					
Earnings (loss) from continuing operations	**$(0.42)**	$2.74	$1.93	$1.64	$1.07
Earnings	**$1.53**	$3.50	$2.91	$2.75	$2.16
Dividends	**$66.931**	$1.60	$1.57	$1.54	$1.515
Average common and common equivalent shares outstanding (in thousands)	**38,262**	41,456	43,312	43,608	44,285
Cash dividends paid:					
On common stock	**$ 1,454,218**	$ 59,598	$ 53,273	$ 51,080	$ 50,390
On preferred stock	**$ 1,944**	$ 4,621	$ 4,972	$ 5,405	$ 5,985
At Year End					
Working capital	**$ 451,609**	$ 985,956	$ 928,427	$ 966,228	$ 882,499
Property, plant and equipment, net	**327,070**	317,238	312,782	270,811	273,677
Capital expenditures:					
Company owned property	**50,966**	40,392	34,239	34,823	39,479
Capitalized leased property	**2,863**	5,533	196	1,388	1,755
Total assets	**1,775,302**	1,830,400	1,741,809	1,587,965	1,533,351
Long-term debt	**1,169,929**	257,327	134,642	127,409	133,311
Debentures	**808,657**	—	—	—	—
Obligations under capital leases	**8,251**	8,864	8,716	7,390	9,383
Shareholders' equity (deficit)	**(1,005,750)**	1,251,337	1,326,215	1,280,153	1,212,105

Board of Directors and Corporate Officers

BOARD OF DIRECTORS

Ronald L. Aylward 1,5
Vice Chairman of the Board of the Company

Zane E. Barnes 2*,3,4,5*
Chairman of the Board, President and Chief Executive Officer of Southwestern Bell Corporation

William E. Cornelius 2,4
Chairman of the Board and Chief Executive Officer of Union Electric Company

Donald E. Lasater 1,2,3*,4,5
Retired Chairman of the Board and Chief Executive Officer of Mercantile Bancorporation Inc.

Marilyn S. Lewis 2
Civic leader and volunteer

Lee M. Liberman 2,3,4*
Chairman of the Board, President and Chief Executive Officer of Laclede Gas Company

Richard B. Loynd
President and Chief Operating Officer of the Company

R. Stuart Moore
Chairman of the Board of The Lane Company, Incorporated

Thomas H. O'Leary 2,3,4,5
President and Chief Executive Officer of Burlington Resources Inc.

Robert H. Quenon 4
President and Chief Executive Officer of Peabody Holding Co., Inc.

Charles J. Rothschild, Jr.
Chairman of the Board of Megastar Apparel Group

Harvey Saligman 1*,5
Chairman of the Board and Chief Executive Officer of the Company

Committees of the Board

1 Executive Committee

2 Audit Committee

3 Executive Compensation and Stock Option Committee

4 Finance Committee

5 Nominating Committee

(*indicates Committee Chairman)

CORPORATE OFFICERS

Harvey Saligman
Chairman of the Board and Chief Executive Officer

Ronald L. Aylward
Vice Chairman of the Board

Richard B. Loynd
President and Chief Operating Officer

Eugene F. Smith
Executive Vice President

Charles J. Rothschild, Jr.
Vice President

R. Stuart Moore
Vice President

Ronald J. Mueller
Vice President

Duane A. Patterson
Secretary

Robert T. Hensley, Jr.
Treasurer

Stanley F. Huck
Controller

Keith E. Mattern
General Counsel and Assistant Secretary

James K. Pendleton
Assistant Secretary

William R. Withrow
Assistant Treasurer

Russell L. Baumann
Assistant Controller

Shareholder Information

Transfer Agents
(Common and Preferred Stock)
Ameritrust Company, N.A.
One Mercantile Center, Suite 2120
St. Louis, Missouri 63101
(314) 241-4002

Morgan Shareholder Services
Trust Company
New York, New York 10249
(212) 587-6434

Registrars
(Common and Preferred Stock)
Ameritrust Company, N.A.
One Mercantile Center, Suite 2120
St. Louis, Missouri 63101
(314) 241-4002

Morgan Shareholder Services
Trust Company
New York, New York 10249
(212) 587-6434

Dividend Disbursing Agent
(Common and Preferred Stock)
Ameritrust Company, N.A.
One Mercantile Center, Suite 2120
St. Louis, Missouri 63101
(314) 241-4002

Exchange Listings
Common Shares are listed on the New York Stock Exchange and the Midwest Stock Exchange. (Trading symbol: ISS)

Trustee, Registrar and Paying Agent for 8.875% Promissary Notes due 1993
The Boatmen's National Bank of St. Louis
Corporate Trust Department
510 Locust Street
St. Louis, Missouri 63101
(314) 436-9581

Trustee, Registrar and Paying Agent for
8.45% Promissory Notes due 1993
8.30% Promissory Notes due 1992
7.95% Promissory Notes due 1991

Trustee:
The Boatmen's National Bank of St. Louis
Corporate Trust Department
510 Locust Street
St. Louis, Missouri 63101
(314) 436-9581

Registrar and Paying Agent:
Bankers Trust Company
Corporate Trust and Agency Group
4 Albany Street
New York, New York 10006
(212) 250-6000 (Shareholder Relations)

Trustee, Registrar and Paying Agent for 13.75% Senior Subordinated Debentures due 2000
First Trust National Association
108 East Fifth Street
St. Paul, Minnesota 55101
(612) 223-7069

Trustee, Registrar and Paying Agent for 14.00% Subordinated Discount Debentures due 2003
Norwest Bank Minnesota N.A.
Sixth Street & Marquette Avenue
Minneapolis, Minnesota 55479
(612) 667-9528

Trustee, Registrar and Paying Agent for 14.50% Junior Pay-in-Kind Subordinated Debentures due 2003
Trustee:
Connecticut National Bank
777 Main Street
Hartford, Connecticut 06115
(203) 722-9082

Registrar and Paying Agent:
Ameritrust Company N.A.
One Mercantile Center, Suite 2120
St. Louis, Missouri 63101
(314) 241-4002

Corporate Offices
101 South Hanley Road
St. Louis, Missouri 63105
(314) 863-1100

Annual Meeting
The Annual Meeting of Shareholders will be held at 10 a.m., Monday, June 26, 1989, at the Clayton Community Center, Two Mark Twain Circle, Clayton, Missouri. Notice of the meeting and a proxy statement will be sent to shareholders in a separate mailing.

Trademarks and Trade Names
The trademarks, trade names and licensed trademarks of INTERCO and its subsidiaries appearing in the Annual Report, are italicized.

Form 10-K Annual Report
A copy of the current Form 10-K filed with the Securities and Exchange Commission can be obtained by writing to the Treasurer of INTERCO at the Corporate Offices.

Independent Accountants
Peat Marwick Main & Co.
1010 Market Street
St. Louis, Missouri 63101
(314) 444-1400

Principal Companies of INTERCO

CORE OPERATING COMPANIES

Footwear Manufacturing and Retailing Group

Converse Inc.
North Reading, Massachusetts

The Florsheim Shoe Company
Chicago, Illinois

Furniture and Home Furnishings Group

Broyhill Furniture Industries, Inc.
Lenoir, North Carolina

The Lane Company, Incorporated
Altavista, Virginia

OTHER OPERATING COMPANIES

Abe Schrader Corporation
New York, New York

Central Hardware Company
St. Louis, Missouri

Devon Apparel
Philadelphia, Pennsylvania

Ethan Allen Inc.
Danbury, Connecticut

Fine's Men's Shops, Incorporated
Norfolk, Virginia

Golde's Department Stores, Inc.
St. Louis, Missouri

Megastar Apparel Group
Paramus, New Jersey

Senack Shoes, Inc.
St. Louis, Missouri

Sky City Stores, Inc.
Asheville, North Carolina

Stuffed Shirt Inc.
New York, New York

United Shirt Distributors, Inc.
Detroit, Michigan

INTERCO INCORPORATED
St. Louis, Missouri